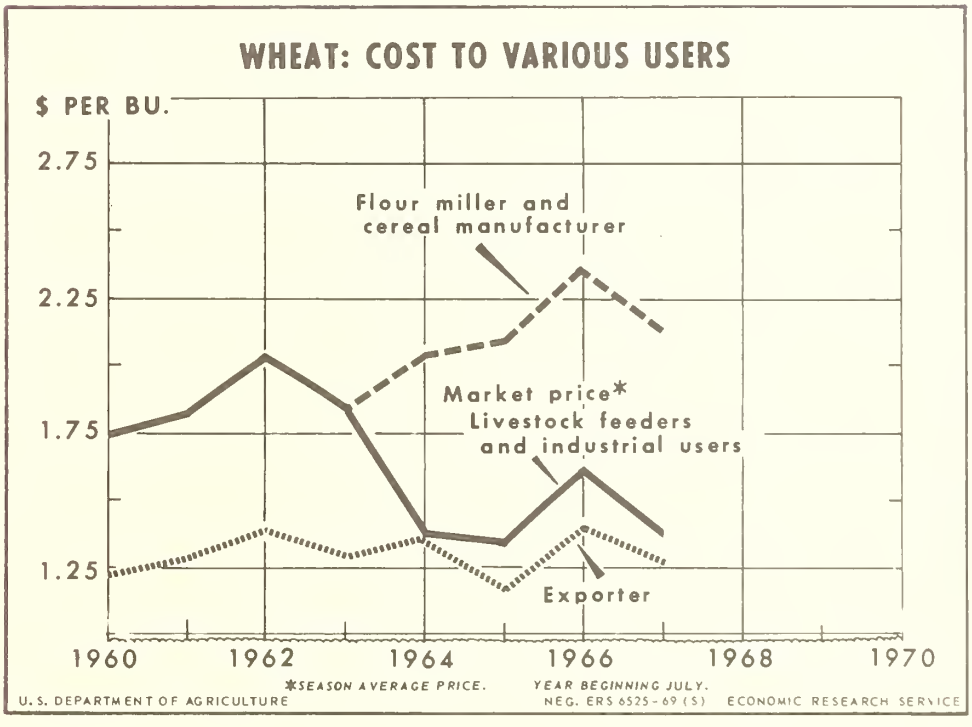
Historic, archived document

Do not assume content reflects current scientific knowledge, policies, or practices.

ERS-418

THE MANY PRICES OF WHEAT

By William R. Askew



TRI AGENCY READING ROOM
MAR 1972
500 12th St., SW. Room 505
Washington D. C. 20250

Reprinted from the Wheat Situation, WS-208, May 1969, by the Economic and Statistical Analysis Division, Economic Research Service.

ERS-418

JUNE 1969

THE MANY PRICES OF WHEAT

by William R. Askew 1/

The domestic wheat program in the United States has been changed significantly in recent years. The major change, in 1963, was in the method of guaranteeing wheat prices. Earlier, there had been little difficulty in understanding wheat prices and producer returns. Some people regard the current program as a two-price or multiple-price plan as opposed to the single price which was the producer's sole return in earlier years. Actually, even today, the market price is the only true price. All other producer returns or costs to buyers have a fixed relation to the market price. This article attempts to explain who gets what and who pays what for wheat.

First let's look at the steps a wheat farmer must take to be enrolled or participate in the wheat program. Each year, usually in the spring or early summer, the Secretary of Agriculture announces an acreage allotment for wheat. The allotment applies to both winter wheat, planted in the fall for harvest the following spring and summer, as well as for spring wheat planted in the spring for harvest in the summer of the same year. The basic national allotment is 59.3 million acres. This corresponds to the 55-million acre minimum national allotment which was in effect for many years. The additional 4.3 million acres results from establishing allotments (not in excess of 15 acres per farm), based on 1959, 1960, and 1961 average acreage, on farms with small or no allotments planting wheat under the 15-acre marketing quota exemption provision.

Basic requirements to be eligible for the loan and payments under the program are: (1) compliance with the acreage allotment; (2) whenever the national allotment is below the basic (59.3 million acres) allotment, diverting an acreage to conservation use equivalent to the difference between the effective farm allotment and the farm allotment that would have been determined under the basic national allotment; and (3) maintenance of the soil conserving base. This conserving base is the average of the soil conserving acreage (including summer fallow and idle cropland) on the farm in 1959 and 1960. Beginning in 1964, (except 1967 and 1968), producers have been required to reduce their allotments from the base level. On occasions, payment was made for this required or mandatory diversion, but in either case the basic compliance conditions prevailed.

There are other secondary requirements for program participation. Except in 1967 and 1968, a voluntary acreage diversion program has been used and of course, payment has been made to induce participation. The rate of payment has varied from year to year depending on the number of acres to be diverted. The allotment has varied from the 59.3 million acre base to increase or decrease production in line with projected demand (export and domestic) for wheat from the crop year involved. The required soil conserving base acreage was reduced in 1967 to correspond with the increase in allotment from the 59.3 million acre base. This permitted the large allotment in 1967. Diverted acreage may not be used for crop production, except in some years for very minor specialized crops, or grazing.

In return for complying with the program provisions, the producer has received a price support loan, and in the years beginning with 1963 a supplementary payment. The price support loan provides a minimum price guarantee. It is a nonrecourse loan in that the producer can deliver the wheat under loan to the Government in full satisfaction of the loan. When prices rise above the loan, producers usually redeem their collateral wheat by paying off the loan, and then sell it in the market. Thus, the producer is assured of a price equal to his local loan rate.

1/ Economic and Statistical Analysis Division, ERS.

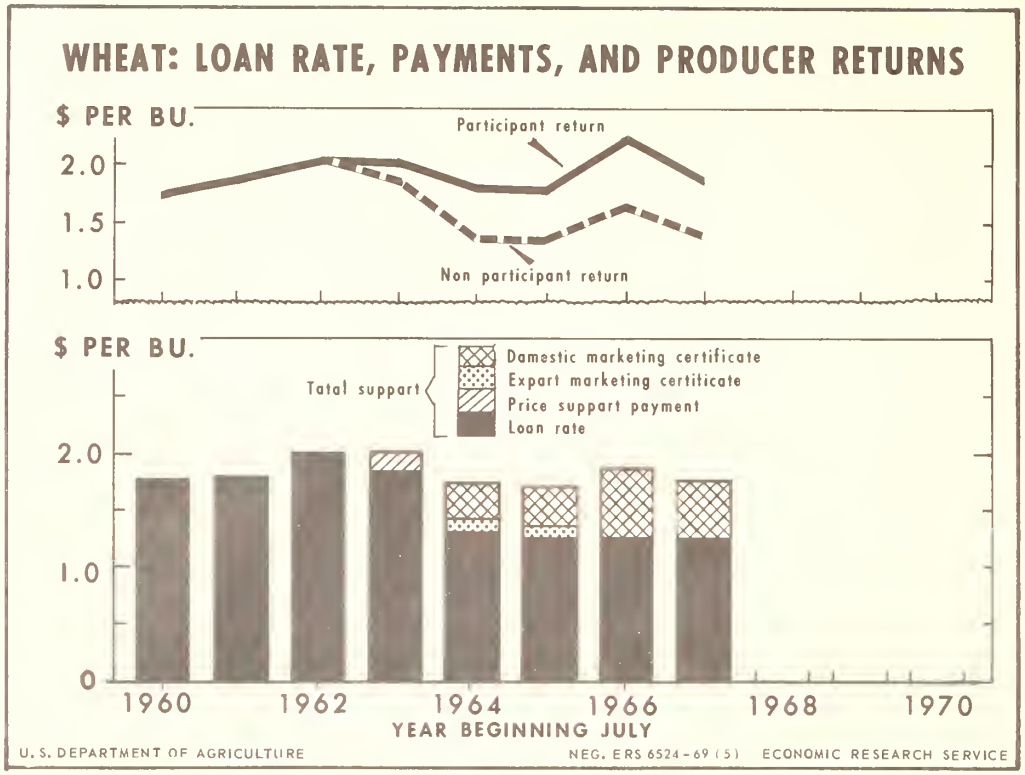


Figure 1

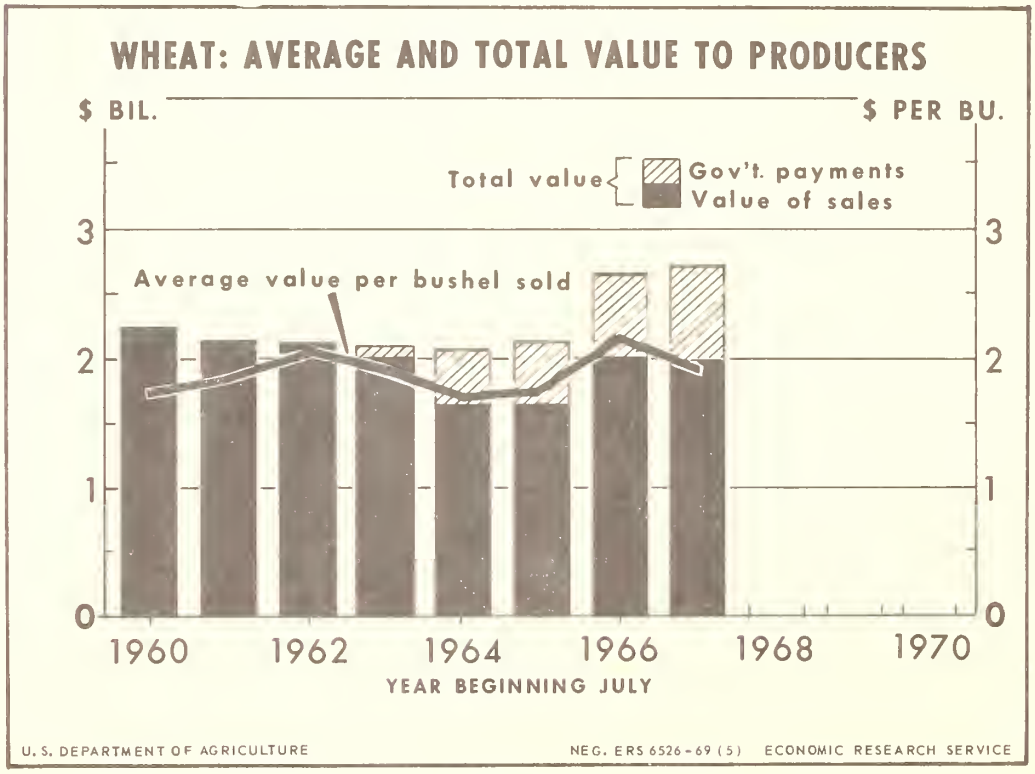


Figure 2

Through 1962 the price support loan was the basic mechanism for providing a guaranteed price. The loan was still the basic but not the sole means of price support in 1963. In that year, producers who reduced their acreage by 20 percent from their allotment received an 18 cent per bushel payment on production from the reduced acreage. Beginning with the 1964 crop, the loan rate was lowered and payments were increased sharply (Fig. 1). This change was brought about by the discontinuation of the mandatory wheat program which had prevailed since 1938. That program let producers vote for a tight control and high support or a weaker control and low support. Except in one instance they choose the former. 1/

The programs beginning with 1964 are not mandatory and have not required a vote or compliance with the allotment. However, the noncomplier receives only the market price and his return has generally been 43 to 59 cents per bushel below that received by the program participant (Fig. 1). Because of this wide spread in returns most of the wheat acreage (around 85 percent) is in the program each year.

Payments to participants in the program are called marketing certificates. In 1964 and 1965, there were both a domestic and export certificate but beginning in 1966 the payment has been solely based on a domestic certificate. Payment to the producer is by check. Payments are computed as a percentage of "normal" production--the farm's assigned yield per acre times the acreage allotment--multiplied by the per bushel certificate value.

These payments do not vary when the farmer's crop fluctuates from the computed "normal" production. However, his harvested acreage cannot be less than the proportion of his acreage covered by certificates if he wants to receive full certificate payment. For example, in 1968 he had to harvest at least 40 percent of his allotment. The exception is in those instances where the crop failed due to natural causes. Certificate payments are derived as shown below.

1/ Producers rejected a wheat referendum for the 1964 crop on May 21, 1963. However, new legislation was passed in April 1964 and established a program for the oncoming 1964 crop.

Wheat Certificate Payments and Proportion of Production or Allotment Covered

Year	Proportion with no payment	Export certificate		Domestic certificate		Average payment
		Proportion	Value	Proportion	Value	
	Pct.	Pct.	Dol./bu.	Pct.	Dol./bu.	Dol./bu.
1964	10	45	.25	45	.70	.428
1965	20	35	.30	45	.75	.442
1966	55	0	---	45	1/1.32	.504
1967	65	0	---	35	1/1.36	.476
1968	60	0	---	40	1/1.38	.552

1/ Difference between July parity price and national average loan rate. Earlier years' payments did not relate to parity.

Now let's look at the cost of wheat to various wheat users. Exporters should first be considered since they are least affected by the changes in the wheat price system. (See cover chart). Their market is the foreign buyer and his consideration is the price of wheat around the world. Although the largest exporter, the United States is only one of a big and growing group of exporters. Therefore, if it is to export wheat, it must sell at the prices mutually determined in world markets. Our domestic prices, even with the lower level of recent years, have generally been above the prices quoted by other exporters. Hence, the United States encourages exports by making a payment to exporters enabling them to sell at the lower world price. Because domestic prices in recent years have declined, the export payment has been reduced and at times suspended.

The wheat users most affected by the current program are the domestic food processor and livestock feeder. The latter pays only the market price and with its lowering has increased his use of wheat in livestock and poultry feeds. This usage averaged around 35 million bushels a year in the early 1960's but has since ranged from 70 to over 150 million bushels a year.

Domestic food processors (flour mills, breakfast food manufacturers, and other processors of wheat for U.S. consumption as human food) pay the USDA a fixed amount of money on every bushel of wheat they process. These payments are a partial offset to the payments made to producers. The remainder of the payment to the producer comes from the U.S. Treasury.

The payment made by the domestic wheat food processor is the difference between $2.00 and the national average loan rate. This method of deriving the processor payment began in 1966. The loan rate for that year and to the present has been $1.25 per bushel and hence the payment has remained at 75 cents per bushel. This is the same as the payment in 1965 but 5 cents greater than in 1964.

One final concept of wheat value should be mentioned. It is the value of wheat both per unit and total. Before the payments entered the picture the average value was the price in the market place and the total value was that average multiplied by the number of bushels producers sold. Thus, to develop average and total values since 1962, payments must be included. The average value beginning in 1963 is misleading, since no one pays that price nor does any producer receive that return (Fig. 2). However, the computed average value is the only measure comparable to the average price which determined value in earlier years. Acreage diversion payments have been excluded from all the calculated producer returns since they are not associated with production but with land taken out of production.